



# Furniture Brands

INTERNATIONAL



*America's largest home furniture manufacturer*

1998 ANNUAL REPORT

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industry and has been rated the number one brand in the industry in terms of consumer awareness by several recent consumer surveys.

Broyhill's product offerings include bedroom, dining room,



and has established a reputation for innovative marketing and quality designs.

Lane's six operating divisions specialize in niche markets including reclining and motion furniture, sleep sofas, bedroom and dining room case goods, occasional pieces, finely tailored upholstered furniture, 18th century reproductions, indoor/outdoor wicker and rattan ensembles, and business/office furniture.

Lane distributes its products in more than 16,000 locations. This distribution includes various

living room, upholstery (stationary and motion), sleep sofas, home office furniture and various occasional collections. Its products encompass a wide range of styles including colonial, country, traditional and contemporary.

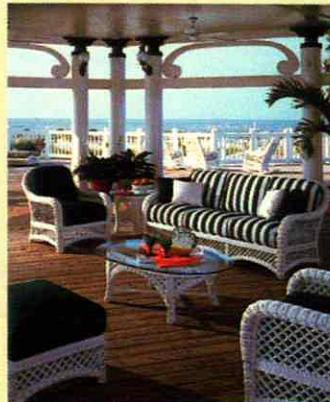
Broyhill products are distributed and sold in more than 6,800 locations primarily through Broyhill Showcase Galleries, Broyhill Independent Dealers and national, regional and local furniture retailers.



**Broyhill**



dedicated gallery programs as well as distribution through independent furniture stores, regional and national chains and department stores.



**Lane**

selected, fancy face veneer patterns and decorative carvings for wood furniture. For upholstered products, these elements include a wide range of frames, fabrics and leathers combined with fringes, cords, pillows, exposed frame finishes and seating options.

Thomasville offers a complete selection of wood furniture and upholstered products in the "best" and "premium" price categories. Major style categories include traditional, American traditional/country, 18th century, European

traditional and casual contemporary. Thomasville also operates other divisions that manufacture and distribute upholstery, assembled promotional furniture and ready-to-assemble (RTA) furniture pieces under separate brand names.

Thomasville has a more focused distribution strategy, selling products through approximately 700 locations including free-standing Thomasville Home Furnishings Stores, in-store galleries and authorized dealers.



**Thomasville**

WHO IS FURNITURE BRANDS?

**Furniture Brands International**

is America's largest home furniture manufacturer.

HOW BROAD IS YOUR PRODUCT LINE?

**Furniture Brands International**

offers more types of furniture, at more price points, than any other residential furniture manufacturer.

HOW DO YOU BUILD YOUR BRANDS?

**Furniture Brands International**

drives its three primary brands — which are among the top six in the furniture industry — by using aggressive advertising and marketing programs directed toward consumers as well as retailers.

WHERE ARE YOUR PRODUCTS FOUND?

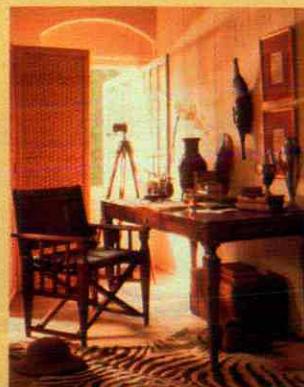
**Furniture Brands International**

products can be found in more than 20,000 locations throughout America and abroad; our distribution network is second-to-none.

**FURNITURE BRANDS INTERNATIONAL IS BROYHILL.** Broyhill was founded in 1926 as The Lenoir Chair Company in Lenoir, North Carolina, and was acquired by the Company in 1980. Its outstanding product quality, widespread brand name recognition and strong distribution make Broyhill a recognized leader in the "good" and "better" price categories — two of the largest segments in the residential furniture market. Broyhill enjoys one of the highest aided and unaided brand name recognition levels in the entire furniture

**FURNITURE BRANDS INTERNATIONAL IS LANE.** Lane was founded by E.H. Lane in 1912 in Altavista, Virginia, as a maker of cedar chests, and was acquired by the Company in 1987. While Lane is still the largest manufacturer of cedar chests in the United States, internal growth and acquisitions have made Lane one of the nation's largest manufacturers and distributors of "better," "best" and "premium" home furniture. Lane is one of the most widely recognized brands in the furniture industry

**FURNITURE BRANDS INTERNATIONAL IS THOMASVILLE.** Thomasville was founded in 1904 in Thomasville, North Carolina, and acquired by Furniture Brands International at the end of 1995. Consumers have recently rated Thomasville as the "highest quality" furniture brand, and management believes Thomasville products contain special design elements that embody the famous "Thomasville Look". These elements include special details, high sheen finishes, original design hardware, hand



## FINANCIAL HIGHLIGHTS

MANCHESTER  
BUSINESS SCHOOL

11 OCT 1999

(In thousands, except per share, employee and statistical data)	Year Ended December 31,		
	1998	1997	1996
<b>From continuing operations:</b>			
Net sales . . . . .	\$1,960,250	\$1,808,276	\$1,696,795
Net earnings <sup>1</sup> . . . . .	90,077	67,053	54,222
As a percentage of net sales . . . . .	4.6%	3.7%	3.2%
Net earnings – as adjusted <sup>2</sup> . . . . .	101,053	79,742	66,919
As a percentage of net sales . . . . .	5.2%	4.4%	3.9%
<b>Per share of common stock (diluted):</b>			
Net earnings <sup>1</sup> . . . . .	\$ 1.67	\$ 1.15	\$ 0.88
Net earnings – as adjusted <sup>2</sup> . . . . .	\$ 1.88	\$ 1.36	\$ 1.08
<b>Financial condition at year-end:</b>			
Working capital . . . . .	\$ 509,148	\$ 482,288	\$ 462,661
Current ratio . . . . .	4.1 to 1	4.5 to 1	4.2 to 1
Total assets . . . . .	1,303,204	1,257,236	1,269,204
Total long-term debt . . . . .	589,200	667,800	572,600
Shareholders' equity . . . . .	\$ 413,509	\$ 323,322	\$ 419,657
Average common shares (diluted) . . . . .	53,809	58,473	61,946
Number of employees . . . . .	20,700	20,700	20,800

<sup>1</sup> Net earnings before nonrecurring gain, net of taxes and extraordinary item, net of taxes.

<sup>2</sup> Adjusted to remove depreciation and amortization related to the 1992 asset revaluation, net of taxes.

### THE COMPANY'S MISSION STATEMENT IS

"To become the residential furniture industry's undisputed leader as an innovative furniture manufacturer and in the process to deliver a significantly improved shareholder value."

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W.G. (Mickey) Holliman

CHAIRMAN OF THE BOARD,  
PRESIDENT AND  
CHIEF EXECUTIVE OFFICER

**F**urniture Brands International had an outstanding year in 1998. Sales, net earnings and net earnings per common share were all at record levels – driven by expanded distribution of our products, improved operating profit margins and efficient management of our capital structure. These results, along with a favorable investment environment, delivered to shareholders a 33% increase in the market value of the Company's common stock for 1998, after a similarly impressive 46% increase in 1997.

Net sales in 1998 were \$1,960.2 million versus \$1,808.3 million reported in 1997, an increase of \$151.9 million or 8.4%. This sales growth, all internally generated, occurred at each operating company and ranged, in varying degrees, across all product lines. We remain committed to aggressively growing market share by: introducing innovative and fashionable products supported by retailer and consumer research; driving our brand names – Broyhill, Lane and Thomasville – through comprehensive and integrated advertising and marketing programs; and expanding dedicated, strategic alliance and non-dedicated distribution with major retailers. With nearly \$2 billion in net sales in 1998, and a meaningful increase expected in 1999, the Company is clearly the largest residential furniture manufacturer in the United States and, arguably, the largest in the world.

Net earnings were \$97.9 million in 1998 compared to \$67.1 million in the prior year – an increase of 46.1%. Excluding the impact of a nonrecurring gain of \$9.4 million (\$7.9 million

after taxes), net earnings increased 34.3%. The improved earnings performance came from the additional sales and, of particular importance, from a substantially higher operating profit margin. The Company's EBITDA margin (earnings before interest expense, income taxes, and depreciation and amortization), which factors out the negative impact of fresh-start accounting, increased to 12.2% in 1998 from 11.2% in 1997. Operating profit margin improvement continues to be a key growth strategy. We are focused on reducing SKU (stock keeping unit) levels throughout the organization and developing vendor alliances to further raise product line profitability and increase working capital turnover. Utilization of our manufacturing asset base, while considerably higher during 1998, still has areas requiring improvement. Finally, our overall cost reduction programs at each operating company are being actively monitored to ensure continued progress is achieved. We expect these efforts to yield further improvement in our operating profit margin going forward.

Net earnings per common share, on a diluted basis and before the nonrecurring gain (\$0.15 per common share), rose 45.2% in 1998 to \$1.67 versus \$1.15 last year. As noted in past years, the Company's financial results continue to be negatively impacted by charges for depreciation and amortization resulting from the 1992 asset revaluation (i.e., fresh-start accounting). Excluding these noncash charges, diluted net earnings per common share would have been \$1.88 and \$1.36 for 1998 and 1997, respectively (before the 1998 nonrecurring gain).

Cash flow from operating activities exceeded \$131 million in 1998 due to the strong earnings performance and our continuing efforts to improve working capital management. The cash flow generated during the year was put to good use. First, approximately \$44 million was spent on capital expenditures. The Company remains dedicated to being a low-cost producer by investing in new manufacturing technologies, while maintaining existing facilities in peak operating condition. Second, we continued our aggressive deleveraging program by repaying almost \$86 million in long-term debt. This deleveraging effort is expected to continue in the future at a similar rate as the Company is focused on strengthening its financial position. Finally, supporting our belief the market value of the Company's common stock does not reflect its true value, approximately \$11 million was invested in the fourth quarter to purchase 525,000 shares on the open market. Additional share repurchases are expected in the future based upon a \$30 million authorization by the Board of Directors.

One of the Company's primary growth strategies consists of strengthening operating management. During 1998, a number of organizational changes were made to address this important area. The most notable of these management moves was the appointment of Dennis R. Burgette to President and Chief Executive Officer of Broyhill Furniture Industries, Inc. effective the beginning of 1999. Dennis, who transferred to Broyhill in mid-1998 from the Company's Lane subsidiary, is another example of the management strength within the Company and its ability to move talented managers among the operating companies to

provide experience and leadership opportunities.

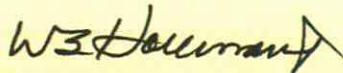
In addition to strengthening operating management during the year, the Company also strengthened the Board of Directors. Dr. Malcolm Portera, President of Mississippi State University, joined the Board in May 1998. Dr. Portera has broad experience in administrative management, business development and strategic planning. We look forward to his thoughtful counsel.

1998 was a great year. The residential furniture industry enjoyed a prosperous period as the overall economic fundamentals (i.e., consumer confidence, consumer spending, employment levels, income growth, interest rates, housing activity, etc.) were, and continue to be, very positive. The Company improved in every important area – manufacturing, marketing, sales, distribution and, most importantly, profitability. We have a more focused, more disciplined and more aggressive management team. Nevertheless, there is more work to be done – and more successes to be achieved.

Our strategic plan is rock solid! There are no changes to be made – just continued, aggressive implementation. This plan has been instrumental in producing 12 consecutive quarters of record operating performance, and we expect continued growth in 1999. The Company's momentum entering into the new year is excellent. Retailer response to our product offerings, marketing and distribution programs continues to be very favorable.

Today, Furniture Brands International is *America's largest home furniture manufacturer*. However, our domestic market share only approaches 10%, and we have barely scratched the surface in the international markets. Thus, the Company has many opportunities to significantly grow sales and profitability. The management and employees are focused on achieving substantial growth and look forward with enthusiasm to working with our suppliers, customers and consumers.

Sincerely,



W.G. (Mickey) Holliman  
Chairman of the Board, President  
and Chief Executive Officer

**F**urniture Brands International offers more types of furniture, at more price points, than any other residential furniture manufacturer.

Furniture Brands International is America's largest home furniture manufacturer. We are a branded consumer products company offering the broadest assortment of products in the industry in all product categories — including case goods, upholstery and occasional furniture. No other company can match our overall offerings at the good, better, best and premium price points. We consistently introduce new and innovative products as part of our growth strategy to increase market share profitably. Regardless of style categories — American traditional/country, 18th century, European traditional or casual contemporary —

Furniture Brands International is well positioned on selection, quality and value.

#### BROYHILL FURNITURE INDUSTRIES, INC.

Broyhill produces case goods, upholstered furniture and occasional pieces positioned at the good and better price points, and offers furniture in colonial, country, traditional and contemporary styles. Broyhill is the best-selling furniture to the mass market, and by itself is one of the world's largest furniture manufacturers.

The company's product strategy is to be a style leader while maintaining the quality and value associated with the Broyhill brand name. That approach grew out of a strategic decision some years ago to transform the company from a manufacturer of basic, low-margin products to a producer of stylish, in-demand, high-margin furniture.

To help determine which new products to bring to market, Broyhill carefully monitors trends in consumer tastes, home building and the home furnishings industry.

In 1998, the *British Empire* collection was introduced by Broyhill as part of its high-end Premier division product offerings. The *British Empire* collection uses dark mahogany wood to create a British Colonial, West Indies look. Dealer reception to this collection has been very strong, making it the most successful Broyhill Premier division placement ever.

Also in 1998, a free-standing kitchen island with bar stools and dining room furniture were added to the highly successful *Windrift* collection of bedroom furniture, occasional pieces and wall systems. *Windrift* has become a top-selling collection for the company.

Two previously introduced upholstery lines continued to do very well. The *hues* collection has become the most successful upholstery introduction in Broyhill history. This collection, which appeals to the growing consumer demand for more casual, family-room furniture, offers 25 frames in five basic fabric colors. The collection is designed to give consumers the ability to easily mix and match any of the frames and fabrics.

At the higher-end, the *Indulgence* collection offers luxurious, plush-styled upholstered furniture with extravagant trims. One of the most successful pieces in this collection is a large, 101-inch-long sofa.

Also in 1998, Broyhill added new entertainment centers and wall units to the *Maison Lenoir* bedroom and dining room collection. This collection, introduced in 1997, was highly successful in 1998 as it became one of Broyhill's best-selling bedroom and dining room groups.



Above: This majestic Victorian poster bed, featuring elegant carvings and sophisticated curves, is part of Broyhill's *British Empire* collection. The collection incorporates elements such as rattan from the South Pacific and East Indian-style carvings, and includes a Raj sideboard and hutch and a Singapore table. Middle: Broyhill's *Windrift* dining group is constructed of pine and ash, solids and veneers, with finishes to create an ocean-side look. The china cabinet features crown molding on top. The group includes special pieces such as a raffia storage chest, a towel cupboard and a kitchen island with bar stools. Bottom: Broyhill's *Indulgence* collection offers eight sofa styles, including this two-on-two sofa, in a variety of fabrics with detailing such as bullion-twisted and braided fringe.



#### LANE FURNITURE INDUSTRIES, INC.

The Lane family of companies includes the nation's second-largest manufacturer of recliners, the largest manufacturer of motion furniture, as well as America's largest manufacturer of cedar chests. Lane also manufactures furniture in a multitude of styles of bedroom, dining room, upholstery, home office, tables and accent pieces priced at the better, best and premium price points.

ACTION, Lane's recliner and motion division, sells products under the Lane brand name. In 1998, it introduced its first all-leather recliner and ottoman. Called *LeatherRest*, it provides the dealer and consumer a high-quality leather product at a very reasonable price with significantly reduced lead times. Reception to this product has been extraordinary, and consumers can look for more all-leather furniture from Lane in 1999. Action had several other important product introductions in 1998. It introduced *Lane Essentials* in one of the industry's leading categories, casual motion furniture. *Lane Essentials* includes innovative features, such as a motion sofa with bun feet, designed to look like a stationary piece. *Lane Expeditions*, a new casual collection of sleep sofas, is offered in three styles and is available as a queen sleep sofa, stationary sofa and loveseat. Action also introduced the *Vintage* collection of reclining chairs, which includes six styles designed to look like stationary chairs. The secret behind this new reclining product line is the ottoman linkage has been redesigned to allow the arms to be closer to the floor for greater comfort.

The LANE DIVISION introduced in 1998 an update to its highly successful Eddie Bauer collection called *American Lifestyles*, which added more than 20 pieces to the original *Eddie Bauer Lifestyles by Lane* collection, the best product introduction for Lane since 1981. The Lane Division also entered a new product

category with the introduction of the *California Club* collection — a full line of very large scale, luxurious, upper-end, casual furniture that incorporates metal, glass, stone and wood pieces.

HICKORY CHAIR is known for its 18th century reproduction pieces. In 1998, the company significantly expanded its *Mount Vernon* collection to coincide with the 200th anniversary of George Washington's death. Hickory Chair also expanded its product line with the introduction of the southern European style *San Marino* collection, designed to look like antique furniture. Hickory Chair's *James River* collection is the oldest and largest collection of 18th century reproductions and adaptations in the industry and continues to achieve impressive sales.

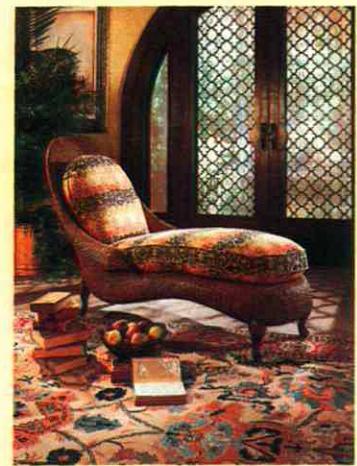
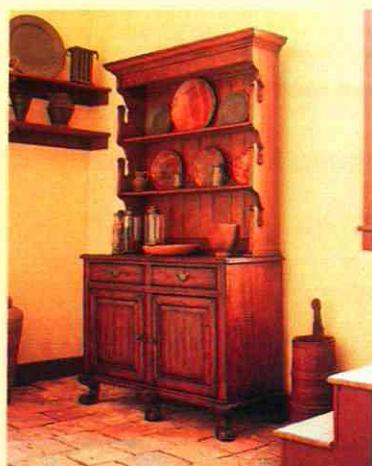
The VENTURE division's *Excursions* collection of high-end, indoor wicker and rattan furniture, featuring living room, dining room, and accent pieces, was the best second-year sales performer ever for a Venture collection. Lane's Venture division also continued to create strong interest in the indoor/outdoor furniture market with newly styled products in its *WeatherMaster* and *Weathercraft* product lines.

PEARSON, one of the top producers of fine-quality, custom-ordered, upholstered furniture, offers more than 500 traditional and transitional styles of premium-quality upholstered furniture coupled with an extraordinary collection of 1,000 of the latest fashion fabrics and leathers.

HBF manufactures premium-quality, high-design office furniture and designs and distributes top-quality textiles. Primarily marketing to Fortune 500 companies, HBF sells complete collections of furniture for boardrooms and lobbies, and office furniture for senior executives. The company also furnishes luxury sky boxes for sports stadiums and arenas around the country.



Above: The *Lane Essentials* collection includes this double reclining sofa and double reclining love seat which feature hidden inside release mechanisms and stationary-scaled frames that provide for comfort and styling. Below left: Lane's new *Eddie Bauer American Lifestyles* collection includes dining room furniture highlighted by meticulous craftsmanship. Below center: The warm cappuccino finish of this *San Marino* collection china hutch by Hickory Chair mixes well with the eclectic designs of other pieces in the group. Below right: The comfort and elegance of this *Lane Excursions* chaise lounge from Venture is one reason this collection had the best second-year sales performance ever for a Venture introduction.



#### THOMASVILLE FURNITURE INDUSTRIES, INC.

Thomasville is positioned at the best to premium end of the furniture market. It manufactures case goods in the American traditional/country, 18th century, European traditional and casual contemporary categories, and upholstery in traditional, American traditional/country and casual contemporary styles.

At the end of 1998, Thomasville made its biggest introduction in 25 years with the *Ernest Hemingway* collection. This collection, inspired by the award-winning author's residences in Kenya, Key West, Havana and Ketchum, Idaho, includes 96 wood and upholstery pieces and has resulted in outstanding initial order volume. The *Ernest Hemingway* collection will ship in 1999 to coincide with the 100th anniversary of the writer's birth.

Thomasville also introduced the *Trafalgar Square* collection of bedroom, dining room and occasional furniture featuring richly grained Honduras mahogany with intricate carvings in a traditional 18th century English style.

Other new product offerings in 1998 were targeted to expand Thomasville's customer base by attracting younger consumers and rounding out the company's product offerings in all furniture categories.

The *Encounter* collection features a light ash finish that appeals to a younger consumer than more traditional Thomasville collections. *Encounter* is a complete line of wood and upholstery products that had a very strong showing in 1998 in its targeted market.

The light pine finish and distinctive Spanish style gives the new *Santiago* collection a

distinctive southwestern feel. It results in the traditional "Thomasville Look" using different, lighter woods.

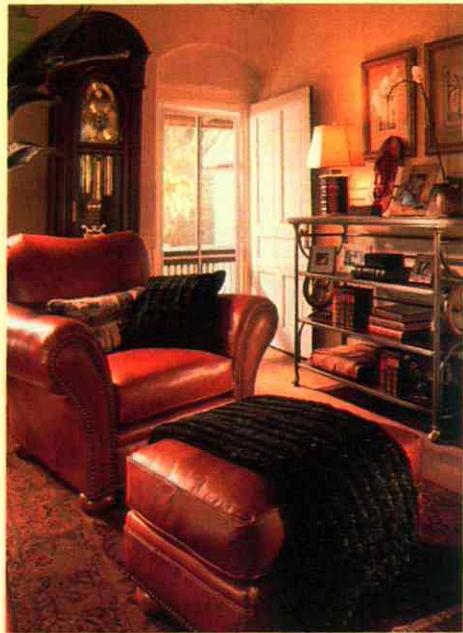
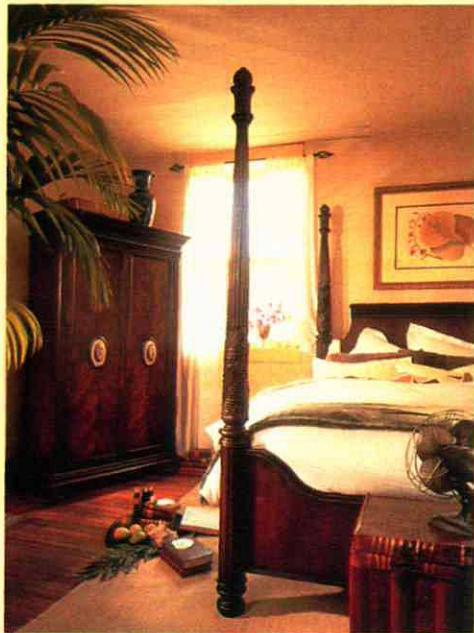
The new *Madison County* collection, manufactured in basic country oak, features a line of high-quality bedroom and dining room furniture appealing to a broader consumer base.

Finally, the *Color Café* line of casual dining furniture provides a "mix and match" collection in five styles — country, French, transitional, casual contemporary and Shaker — and 12 colors. *Color Café* includes tables with birch wood tops, chairs, china cabinets and bar stools.

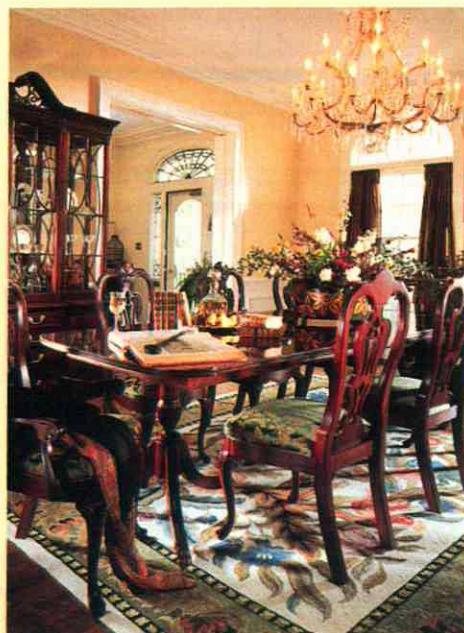
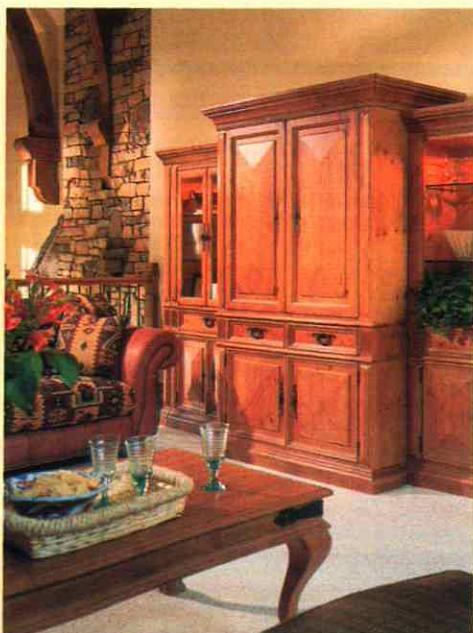
Traditionally a case goods manufacturer, Thomasville has made a concerted effort to grow its upholstery business. This sound business strategy has helped Thomasville gain greater penetration in the upholstery category, which represents more than 40 percent of furniture industry shipments. Management believes that Thomasville is the largest manufacturer of eight-way, hand-tied custom upholstery in the world. In addition, Thomasville also is the industry's largest producer of carved furniture, and the company is recognized as the leading chair manufacturer in the industry.

Effective January 1, 1999, the operations of Highland House, formerly a division of Broyhill, were transferred to Thomasville. This transfer of operations will benefit Thomasville due to the additional capacity available to service its rapidly growing upholstery business. The Highland House operations will be enhanced through increased utilization of its capacity and through a strategic fit with a company sharing a similar niche in the marketplace.

*Furniture Brands International markets a breadth of product offerings unparalleled in the industry. Our product quality and style leadership, together with the power of our brands and strength of our distribution, make us the best choice for fulfilling the consumer's furniture needs.*



Above left: The Key West poster bed and companion pieces from the *Ernest Hemingway* Collection comprise one of four styles influenced by residences in which the award-winning author lived. Above right: This spacious, rugged leather chair and ottoman have been dubbed the "Papa Hemingway" and is an example of the collection's fabulous upholstery offerings. Below left: This entertainment unit and occasional table feature the light pine finish with Spanish design motifs that give Thomasville's *Santiago* collection its distinctive southwestern feel. Below right: Richly grained Honduras mahogany in this dining room from the *Trafalgar Square* collection highlights the intricate carvings that are a hallmark of all Thomasville furniture.



**F**urniture Brands International drives its three primary brands — which are among the top six in the furniture industry — by using aggressive advertising and marketing programs directed toward consumers as well as retailers.

Furniture Brands International uses an integrated strategy of television, radio and print advertising, tied to marketing events, consumer telephone help lines and Internet Web sites, to drive its brand names. Our spending on these activities was at record levels. 1998 marked the first time the Company sponsored a national



sporting event, "An Evening with the Ice Girls," a professional ice-skating show, initially broadcast on CBS and

later on ESPN, featuring 10 different commercials advertising our products. In addition, the ice-skating rink displayed the logos of our brands, so fans at the event and TV viewers saw our brand names as the skaters performed.

Another first in 1998 — each of our three operating companies used television advertising, including national cable networks as well as specific regional channels. On the print side, we continued to use shelter and other magazines to promote our brands to the consumer.

We literally "drove" our brands last year by increasing the advertising on our trucking fleet, a tactic that will increase our advertising impressions by more than 500 million a year. Finally, virtually all of our operating companies have established Web sites, so we are beginning to use the Internet in our marketing strategies.

BROYHILL employed television advertising for the first time during 1998, and that played a significant role in driving business. One commercial was a brand-builder that carried the tagline: "Every 30 seconds some-



one chooses Broyhill." To emphasize the breadth of its product offerings, the commercial flashes 123 product shots in just a few seconds.

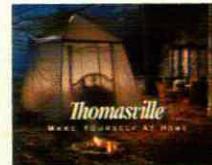
Broyhill also advertises in most of the top 10 magazines based on circulation, including shelter and non-shelter publications.

LANE was the sole sponsor of "Rock-n-Roll Gymnastics," which originally aired on ESPN last year and included eight different Lane commercials. This program has had seven national airings on ESPN, with the original broadcast during the Lane national sale in October.

Each of the Lane divisions advertises extensively in trade and consumer publications targeting various niche markets.

THOMASVILLE geared its marketing in 1998 to attract younger consumers to its products, and included placements in publications such as *InStyle* and *Entertainment Weekly*. Like Broyhill and Lane, Thomasville aired various television commercials in 1998. Throughout the year, it advertised regionally in key markets including Boston and Los Angeles. Decisions on where to use the television advertising are made on a market-by-market basis with the participation of individual stores.

Expect more television ads by Thomasville as it continues its successful efforts to attract younger consumers.



Create new traditions with Maison Lenoir

The Maison Lenoir collection from Broyhill is a mixture of traditional and modern elements. The bedroom features a four-poster bed with a hand-carved wooden headboard and footboard, accented with a floral chenille fabric. The dresser and armoire are made of solid cherry wood and feature hand-carved floral and leaf patterns. The sofa and chair are upholstered in a soft, light-colored fabric with a subtle floral pattern. The coffee table is made of solid cherry wood and features a glass top. The rug is a light-colored area rug with a subtle floral pattern.

**Maison Lenoir**  
Broyhill

Cozy corners.

The new Richland Ridge Bedroom from Lane® brings the entire family together. The room is a great example of reclining versatility. You can recline in a chair, a sofa, or a loveseat. The room is also equipped with additional features like a coffee table and the lower back-massage unit with heat. For a free buyer's guide and the dealer nearest you, call toll-free 1-800-632-6952. You may also visit our web site at [www.lane.com](http://www.lane.com).

**Lane®**

THE WAY WE WANT TO LIVE

**Eddie Bauer LIFESTYLES**  
Lane AMERICAN LIFESTYLES COLLECTION

"You always know that you are home when a house speaks to you... and they do speak, the best of them."

—A Beautiful Home, Marianne Gugher

**Thomasville**  
MAKE YOURSELF AT HOME™

For centuries, great artists and writers have all been inspired by the warmer beauty and power of our majestic woods. Since 1818, Thomasville has celebrated this history with an exceptional collection of furniture for the bedroom, dining room, and living room. Crafted in historic American cities and rustic towns such as the Tobacco Safe embodies the early going lifestyle and craftsmanship of the 1800s. The Thomasville Bedroom Collection is a collection of bedroom furniture that can be used in any room, the Frank Quarter-Ecclesiastical Table features a hand-carved inscription; illuminated leather and hand-painted glass. For more information on the Oceanside Eddie Bauer Collection or the Thomasville website, contact your call or at 1-800-420-1028 or visit our website at [www.thomasville.com](http://www.thomasville.com).

Top left: In 1998, surveys found that Broyhill was the most recognized full-line furniture brand with both aided and unaided recall. To introduce the *Maison Lenoir* collection, Broyhill ran four-page brochure inserts in magazines complemented by television advertising. Top right: Lane's Action division uses print advertising extensively as part of its integrated marketing approach to drive its various product lines. Bottom left: Advertising helped propel *Eddie Bauer Lifestyles* by Lane to such success that Lane has expanded the product line with *American Lifestyles*. Bottom right: Thomasville continued its efforts to attract new consumers by placing stylish, eye-catching ads in publications such as *InStyle* and *Entertainment Weekly*.

# Furniture Brands International products can be found in more than 20,000 locations throughout America and abroad; our distribution network is second-to-none.

Furniture Brands International has the largest distribution network in the industry, more than double that of our nearest competitor. The Company divides its distribution into three key components: dedicated, strategic alliance and non-dedicated.

Dedicated space represents approximately 50 percent of our business. One of our top business strategies is to aggressively pursue more dedicated floor space, which typically boosts sales 20 percent above sales in non-dedicated space. At the end of 1998, the Company had approximately 8.9 million square feet of dedicated floor space in almost 1,800 galleries, furniture centers, boutiques and Thomasville stores.

Our strategic alliance with Havertys, (one of the top five furniture retailers in the country), was major distribution news in the furniture industry in 1998. Under the agreement, our Company's products, which had occupied 18 percent of Haverty's total showroom floor space, will occupy 50 percent by early 1999, representing over 1.5 million square feet of locked-in distribution. The alliance already has produced significant sales increases for each of our brands.

Counting non-dedicated space, consumers can find our products in more than 20,000 retail locations covering all 50 states and more than 55 countries.

The Company's strategy is to expand its distribution — dedicated, strategic alliance and non-dedicated — both domestically and internationally.

BROYHILL distributes its furniture to more than 6,800 retail outlets. In 1998, it opened its 500th Broyhill Furniture Center, each of which dedicates more than 2,000 square feet to Broyhill furniture. Retailers operate more than 350 Broyhill Showcase Galleries — typically 7,500 square feet in size.

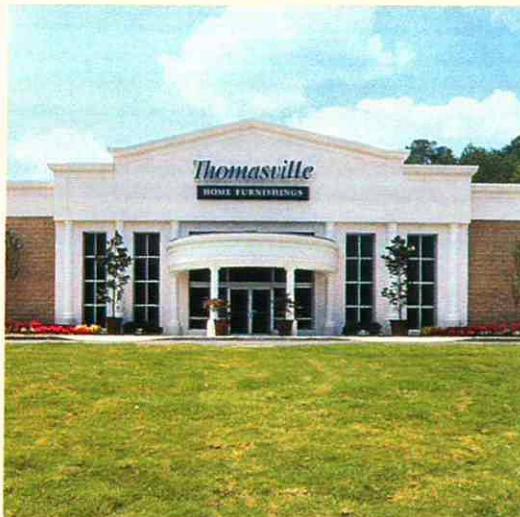
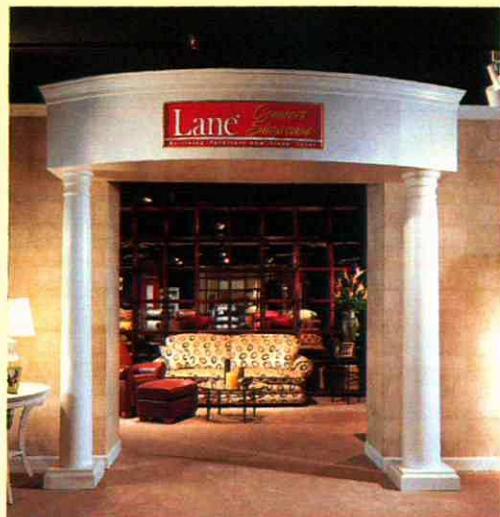
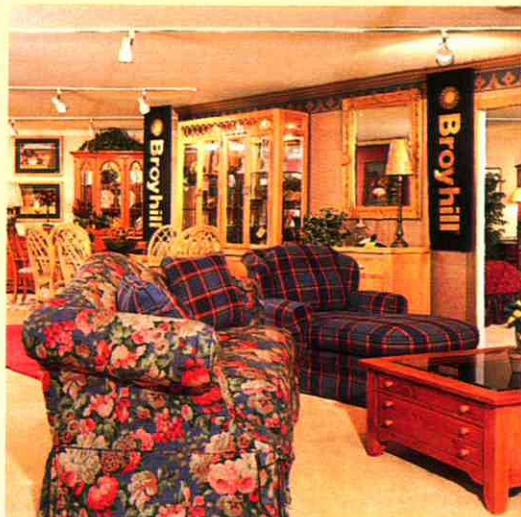
Broyhill is in the process of adjusting its management organization and marketing programs (e.g., Broyhill Express — a quick-ship program) to grow both its domestic and international distribution.

LANE distributes its products to more than 16,000 locations, including 255 Lane Comfort Showcase Galleries, 52 Lane Galleries, 162 Lane Cedar Boutiques, 51 Raymond Waites Galleries and 51 Hickory Chair Galleries, an increase of almost 20 percent in the number of dedicated distribution outlets from 1997. Internationally, the Lane companies have more than 550 retail locations in more than 55 countries.

Lane's emphasis on new product development such as Action's *LeatherRest* recliner, Lane Division's *Eddie Bauer American Lifestyles* collection and Venture's *Excursion* group, helped Lane expand distribution during 1998 to new dealers that are carrying Lane furniture for the first time while also gaining back dealers who had carried Lane products previously.

THOMASVILLE, with its more focused distribution, distributes its products through 105 independently owned Thomasville Home Furnishings Stores, which average 15,000 square feet, 249 Thomasville Galleries and nearly 300 dealers. In May, a Thomasville store opened in Shanghai, China. By year-end, more than 10 international Thomasville stores were open in Canada, Latin America and Asia.

To grow its distribution, Thomasville is concentrating on obtaining the best store and gallery locations and partnering with the furniture industry's premier dealers. A key growth strategy is to increase the number of stores to 200 within four years. New product and marketing programs coupled with strong advertising should support this effort.



**LARGEST AND GROWING  
DISTRIBUTION NETWORK**  
*(as of December 31, 1998)*

**DEDICATED**

- 1,678 Galleries, Furniture Centers and Boutiques — over 7.3 million square feet
- 105 Thomasville Home Furnishings Stores — over 1.6 million square feet

**STRATEGIC ALLIANCE**

- Haverty Furniture Companies, Inc. — over 1.5 million square feet

**NON-DEDICATED**

- 20,000 + retail locations  
(national, regional, independent)

Furniture Brands International has the largest distribution network — dedicated, strategic alliance and non-dedicated — in the industry, with customers in all 50 states and more than 55 countries. Top left: Broyhill opened its 500th Broyhill Furniture Center last year, a smaller version of the Broyhill Showcase

Galleries that now are in more than 350 retail stores. Top right: Lane had 571 galleries and boutiques throughout its divisions at the end of 1998.

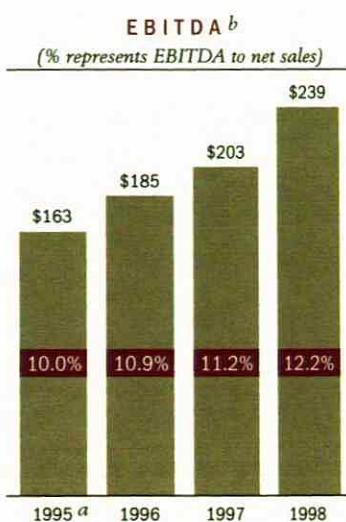
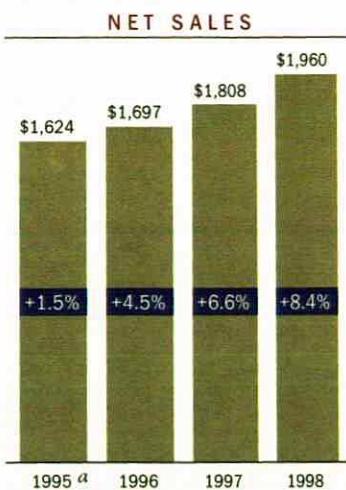
Bottom left: There were 105 independently owned Thomasville Home Furnishings Stores and 249 Thomasville Galleries open at year-end.

**DISTRIBUTION NETWORK EXPANSION**

During February 1999, the Company announced two significant additions to its growing distribution network. First, the Company entered into a cooperative effort with Benchmark Home

Furnishings, Inc. to develop a 160,000-square-foot store in Kansas City dedicated exclusively to products manufactured by Furniture Brands International. Also, the Company announced a strategic alliance with Kittle's

Home Furnishings, Inc., a major Midwest retailer, to expand its commitment to products manufactured by the Company. These events demonstrate the success of the Company's distribution expansion strategy.

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<sup>a</sup> Pro forma for Thomasville acquisition.

<sup>b</sup> Earnings before interest expense, income taxes, depreciation and amortization.

<sup>c</sup> Excludes nonrecurring gains and extraordinary items.

MANAGEMENT'S DISCUSSION AND ANALYSIS  
OF RESULTS OF OPERATIONS AND FINANCIAL CONDITION

RESULTS OF OPERATIONS

As an aid to understanding the Company's results of operations on a comparative basis, the following table has been prepared to set forth certain statements of operations and other data for 1998, 1997 and 1996.

(Dollars in millions)	Year Ended December 31,					
	1998		1997		1996	
	Dollars	% of Net Sales	Dollars	% of Net Sales	Dollars	% of Net Sales
Net sales	\$1,960.2	100.0%	\$1,808.3	100.0%	\$1,696.8	100.0%
Cost of operations	1,406.4	71.7	1,319.5	73.0	1,228.4	72.4
Selling, general and administrative expenses	314.8	16.1	286.1	15.8	283.4	16.7
Depreciation and amortization	55.5	2.8	56.0	3.1	54.1	3.2
Earnings from operations	183.5	9.4	146.7	8.1	130.9	7.7
Interest expense	43.5	2.2	42.7	2.4	45.2	2.7
Other income, net	12.1	0.6	3.3	0.2	2.6	0.2
Earnings before income tax expense and extraordinary item	152.1	7.8	107.3	5.9	88.3	5.2
Income tax expense	54.2	2.8	40.2	2.2	34.1	2.0
Earnings before extraordinary item	\$ 97.9	5.0%	\$ 67.1	3.7%	\$ 54.2	3.2%
Gross profit <sup>1</sup>	\$ 515.5	26.3%	\$ 450.7	24.9%	\$ 431.5	25.4%

<sup>1</sup>The Company believes that gross profit provides useful information regarding a company's financial performance. Gross profit has been calculated by subtracting cost of operations and the portion of depreciation associated with cost of goods sold from net sales.

(Dollars in millions)	Year Ended December 31,		
	1998	1997	1996
Net sales	\$1,960.2	\$1,808.3	\$1,696.8
Cost of operations	1,406.4	1,319.5	1,228.4
Depreciation (associated with cost of goods sold)	38.3	38.1	36.9
Gross profit	\$ 515.5	\$ 450.7	\$ 431.5

**MANAGEMENT'S DISCUSSION AND ANALYSIS  
OF RESULTS OF OPERATIONS AND FINANCIAL CONDITION**

*Year Ended December 31, 1998 Compared to Year Ended December 31, 1997*

Net sales for 1998 were \$1,960.2 million compared to \$1,808.3 million for 1997, an increase of \$151.9 or 8.4%. The improved sales performance for 1998 occurred at each operating company and ranged, in varying degrees, across all product lines. The increase in net sales was achieved through continued introductions of new products, emphasis on the Company's brand names and expansion of distribution.

Cost of operations for 1998 was \$1,406.4 million compared to \$1,319.5 million for 1997, an increase of 6.6%. Cost of operations as a percentage of net sales decreased from 73.0% for 1997 to 71.7% in 1998 primarily due to improved manufacturing capacity utilization, reduced stock keeping units and ongoing cost reduction programs.

Selling, general and administrative expenses increased to \$314.8 million in 1998 from \$286.1 million in 1997, an increase of 10.0%. As a percentage of net sales, selling, general and administrative expenses increased from 15.8% for 1997 to 16.1% for 1998 because of tight spending controls implemented during the fourth quarter of 1997 to help offset an operational restructuring at Thomasville and a temporary promotional product mix change.

Depreciation and amortization for 1998 was \$55.5 million compared to \$56.0 million in 1997, a decrease of 0.9%. The amount of depreciation and amortization attributable to the "fresh-start" reporting was \$13.7 million and \$16.4 million in 1998 and 1997, respectively.

Interest expense for 1998 totaled \$43.5 million compared with \$42.7 million in 1997. The increase in interest expense reflects additional long-term debt incurred at the end of the second quarter of 1997 to finance the Company's repurchase of approximately 10.8 million shares of its common stock.

Other income, net for 1998 totaled \$12.1 million compared to \$3.3 million for 1997. For 1998, other income consisted of interest on short-term investments of \$0.9 million, a cash dividend (nonrecurring) of \$9.4 million received by the Company relating to its minority investment in a company which leases exhibition space to furniture and accessory manufacturers, and other miscellaneous income and expense items totaling \$1.8 million.

Income tax expense for 1998 totaled \$54.2 million, producing an effective tax rate of 35.6% compared with an effective tax rate of 37.5% for 1997. The effective tax rates for both periods were adversely impacted by certain nondeductible expenses incurred and provisions for state and local income taxes. The effective tax rate for 1998 was favorably impacted by the reduced effect of the nondeductible expenses as a percentage of pretax earnings and the nontaxable portion of the \$9.4 million cash dividend.

Net earnings per common share on a diluted basis were \$1.82 and \$1.15 for 1998 and 1997, respectively. Weighted average shares outstanding used in the calculation of net earnings per common share on a basic and diluted basis were 52,095,000 and 53,809,000 in 1998, respectively, and 56,438,000 and 58,473,000 in 1997, respectively.

Gross profit for 1998 was \$515.5 million compared with \$450.7 million in 1997, an increase of 14.4%. The increase in gross profit margin to 26.3% in 1998 from 24.9% in 1997 was due to improved manufacturing capacity utilization, reduced stock keeping units and ongoing cost reduction programs.

*Year Ended December 31, 1997 Compared to Year Ended December 31, 1996*

Net sales for 1997 were \$1,808.3 million compared to \$1,696.8 million for 1996, an increase of \$111.5 or 6.6%. The improved sales performance for 1997 occurred at each operating company and ranged, in varying degrees, across all product lines. The increase in net sales was achieved through continued introductions of new products, emphasis on the Company's brand names and expansion of distribution.

Cost of operations for 1997 was \$1,319.5 million compared to \$1,228.4 million for 1996, an increase of 7.4%. Cost of operations as a percentage of net sales increased from 72.4% for 1996 to 73.0% in 1997 primarily due to the negative impact of a manufacturing plant closing and related production realignment at Thomasville.

Selling, general and administrative expenses increased to \$286.1 million in 1997 from \$283.4 million in 1996, an increase of 0.9%. As a percentage of net sales, selling, general and administrative expenses decreased from 16.7% for 1996 to 15.8% for 1997 reflecting the Company's ongoing implementation of cost control and reduction programs.

Depreciation and amortization for 1997 was \$56.0 million compared to \$54.1 million in 1996, an increase of 3.5%. The amount of depreciation and amortization attributable to the "fresh-start" reporting was \$16.4 million and \$16.3 million in 1997 and 1996, respectively.

Interest expense for 1997 totaled \$42.7 million compared with \$45.2 million in 1996. The reduced interest expense reflects lower long-term debt balances during the first six months of the year, offset partially by additional long-term debt incurred at the end of the second quarter to finance the Company's repurchase of approximately 10.8 million shares of its common stock.

Other income, net for 1997 totaled \$3.3 million compared to \$2.6 million for 1996. For 1997, other income consisted of interest on short-term investments of \$0.9 million and other miscellaneous income and expense items totaling \$2.4 million.

Income tax expense for 1997 totaled \$40.2 million, producing an effective tax rate of 37.5% compared with an effective tax rate of 38.6% for 1996. The effective tax rates for both periods were adversely impacted by certain nondeductible expenses incurred and provisions for state and local income taxes.

Earnings per common share before extraordinary item on a diluted basis were \$1.15 and \$0.88 for 1997 and 1996, respectively. Weighted average shares outstanding used in the calculation of net earnings per common share on a basic and diluted basis were 56,438,000 and 58,473,000 in 1997, respectively, and 59,172,000 and 61,946,000 in 1996, respectively.

Gross profit for 1997 was \$450.7 million compared with \$431.5 million in 1996, an increase of 4.5%. The decrease in gross profit margin to 24.9% in 1997 from 25.4% in 1996 was primarily due to the previously noted manufacturing plant closing and related production realignment at Thomasville.

## MANAGEMENT'S DISCUSSION AND ANALYSIS OF RESULTS OF OPERATIONS AND FINANCIAL CONDITION

### FINANCIAL CONDITION AND LIQUIDITY

#### *Liquidity*

Cash and cash equivalents at December 31, 1998 totaled \$13.2 million compared to \$12.3 million at December 31, 1997. For 1998, net cash provided by operating activities totaled \$131.3 million. Net cash used by investing activities totaled \$43.1 million. Net cash used in financing activities totaled \$87.2 million, including the net payment of \$85.8 million of long-term debt.

Working capital was \$509.1 million at December 31, 1998 compared to \$482.3 million at December 31, 1997. The current ratio was 4.1 to 1 at December 31, 1998 compared to 4.5 to 1 at December 31, 1997. The modest increase in working capital between years is primarily the result of the Company's focus on efficient management of individual working capital components.

At December 31, 1998, long-term debt totaled \$589.2 million compared to \$667.8 million at December 31, 1997. The decrease in indebtedness was funded by cash flow from operations, partially offset by the issuance of industrial revenue bonds for the construction of a manufacturing plant addition at Action Industries, Inc. (subsidiary of Lane Furniture Industries, Inc.). The Company's debt-to-capitalization ratio was 58.8% at December 31, 1998 compared to 67.4% at December 31, 1997.

#### *Financing Arrangements*

To meet short-term capital and other financial requirements, the Company maintains a \$600.0 million revolving credit facility as part of its Secured Credit Agreement with a group of financial institutions. The revolving credit facility allows for both issuance of letters of credit and cash borrowings. Letter of credit outstandings are limited to no more than \$60.0 million. Cash borrowings are limited only by the facility's maximum availability less letters of credit outstanding. At December 31, 1998, there were \$370.0 million of cash borrowings outstanding under the revolving credit facility and \$41.0 million in letters of credit outstanding, leaving an excess of \$189.0 million available under the revolving credit facility.

In January 1998, in order to reduce the impact of changes in interest rates on its floating rate long-term debt, the Company entered into a four-year interest rate swap agreement having a total notional amount of \$300.0 million. The swap agreement effectively converts a portion of the Company's floating rate long-term debt to a fixed rate. The Company pays the counterparties a fixed rate of 5.50% per annum and receives payment based upon the floating three-month LIBOR rate.

The Company believes its Secured Credit Agreement, together with cash generated from operations, will be adequate to meet liquidity requirements for the foreseeable future.

*Market Risk*

The Company is exposed to market risk from changes in interest rates. The Company's exposure to interest rate risk consists of its floating rate secured credit agreement. Interest rate swaps are used to reduce the Company's exposure to increases in interest rates.

*Year 2000*

The Company has completed a comprehensive review of all software, hardware and equipment that could potentially be affected by the year 2000 issue and adopted a year 2000 plan to meet the needs of its customers and business partners. The results of the review indicate that the Company will be year 2000 compliant before the year 2000. At this time remediations are being implemented and initial testing of the remediations has begun. The total cost for year 2000 compliance activity will not be material to the Company's results of operations and financial position. The Company is also in the process of verifying compliance of critical suppliers with year 2000 standards. There can be no assurance that another company's failure to ensure year 2000 compliance will not have a material adverse effect on the Company, however this is a circumstance not currently expected to occur. The Company will develop and implement contingency plans, if necessary, in the event it appears that it or its key suppliers will not be year 2000 compliant and such noncompliance is expected to have a material adverse impact on the operations of the Company.

*Recently Issued Statements of Financial Accounting Standards*

In June, 1998 the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 133 (SFAS No. 133) "Accounting for Derivative Instruments and Hedging Activities". This statement standardizes the accounting for derivative instruments by requiring that an entity recognize these items as assets and liabilities in the statement of financial position and measure them at fair value. SFAS No. 133 becomes effective for fiscal years beginning after June 15, 1999; however, the Company does not believe that the adoption of this statement will have a material impact on its financial statements.

*Forward-Looking Statements*

From time to time, the Company may make statements which constitute or contain "forward-looking" information as that term is defined in the Private Securities Litigation Reform Act of 1995 or by the Securities and Exchange Commission in its rules, regulations and releases. The Company cautions investors that any such forward-looking statements made by the Company are not guarantees of future performance and that actual results may differ materially from those in the forward-looking statements. The impact of the year 2000 on the Company's order, production, distribution and financial systems and the systems of its suppliers and customers is a factor which could cause actual results to differ materially from estimates contained in the Company's forward-looking statements.

**CONSOLIDATED BALANCE SHEETS**

(Dollars in thousands)	<i>December 31, 1998</i>	<i>December 31, 1997</i>
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 13,220	\$ 12,274
Receivables, less allowances of \$18,333 (\$13,793 at December 31, 1997)	324,164	293,975
Inventories (Note 3)	307,382	287,046
Prepaid expenses and other current assets	31,107	25,214
Total current assets	675,873	618,509
Property, plant and equipment:		
Land	16,757	16,758
Buildings and improvements	188,874	178,245
Machinery and equipment	294,282	264,689
	499,913	459,692
Less accumulated depreciation	206,136	165,631
Net property, plant and equipment	293,777	294,061
Intangible assets (Note 4)	316,998	330,549
Other assets	16,556	14,117
	<b>\$1,303,204</b>	<b>\$1,257,236</b>
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
Current liabilities:		
Accounts payable	\$ 67,381	\$ 52,141
Accrued employee compensation	35,758	29,430
Accrued interest expense	5,608	7,451
Other accrued expenses	57,978	47,199
Total current liabilities	166,725	136,221
Long-term debt (Note 5)	589,200	667,800
Other long-term liabilities	133,770	129,893
Shareholders' equity:		
Preferred stock, authorized 10,000,000 shares, no par value – issued, none	—	—
Common stock, authorized 100,000,000 shares, \$1.00 stated value – issued 52,277,066 and 52,003,520 shares at December 31, 1998 and 1997 (Note 6)	52,277	52,003
Paid-in capital	127,513	124,595
Retained earnings	244,662	146,724
Treasury stock at cost (525,000 shares at December 31, 1998)	(10,943)	—
Total shareholders' equity	413,509	323,322
	<b>\$1,303,204</b>	<b>\$1,257,236</b>

See accompanying notes to consolidated financial statements.

**CONSOLIDATED STATEMENTS OF OPERATIONS**

<i>(Dollars in thousands except per share data)</i>	<i>Year Ended December 31,</i>		
	<i>1998</i>	<i>1997</i>	<i>1996</i>
Net sales	\$1,960,250	\$1,808,276	\$1,696,795
Costs and expenses:			
Cost of operations	1,406,434	1,319,455	1,228,355
Selling, general and administrative expenses	314,837	286,086	283,432
Depreciation and amortization (includes \$13,670, \$16,369 and \$16,285 related to fair value adjustments)	55,469	55,995	54,082
Earnings from operations	183,510	146,740	130,926
Interest expense	43,455	42,747	45,217
Other income, net	12,088	3,261	2,583
Earnings before income tax expense and extraordinary item	152,143	107,254	88,292
Income tax expense (Note 7)	54,205	40,201	34,070
Earnings before extraordinary item	97,938	67,053	54,222
Extraordinary item – early extinguishment of debt, net of tax benefit (Note 9)	—	—	(7,417)
Net earnings	\$ 97,938	\$ 67,053	\$ 46,805
Net earnings per common share – basic (Note 6):			
Earnings before extraordinary item	\$ 1.88	\$ 1.19	\$ 0.92
Extraordinary item – early extinguishment of debt	—	—	(0.13)
Net earnings per common share – basic	\$ 1.88	\$ 1.19	\$ 0.79
Net earnings per common share – diluted (Note 6):			
Earnings before extraordinary item	\$ 1.82	\$ 1.15	\$ 0.88
Extraordinary item – early extinguishment of debt	—	—	(0.12)
Net earnings per common share – diluted	\$ 1.82	\$ 1.15	\$ 0.76

See accompanying notes to consolidated financial statements.

**CONSOLIDATED STATEMENTS OF CASH FLOWS**

<i>(Dollars in thousands)</i>	<i>Year Ended December 31,</i>		
	<i>1998</i>	<i>1997</i>	<i>1996</i>
<b>Cash flows from operating activities:</b>			
Net earnings	\$ 97,938	\$ 67,053	\$ 46,805
Adjustments to reconcile net earnings to net cash provided by operating activities:			
Net loss on early extinguishment of debt	—	—	7,417
Depreciation of property, plant and equipment	43,409	43,935	42,022
Amortization of intangible and other assets	12,060	12,060	12,060
Noncash interest expense	2,107	1,297	2,042
Increase in receivables	(30,189)	(10,558)	(7,301)
Increase in inventories	(20,336)	(5,939)	(11,430)
(Acrease) decrease in prepaid expenses and intangible and other assets	(3,055)	3,655	13,695
Increase (decrease) in accounts payable, accrued interest expense and other accrued expenses	29,704	(7,405)	33,710
Increase (decrease) in net deferred tax liabilities	2,624	(8,056)	(7,972)
Increase (decrease) in other long-term liabilities	(2,956)	7,669	(15,628)
Net cash provided by operating activities	131,306	103,711	115,420
<b>Cash flows from investing activities:</b>			
Proceeds from the disposal of assets	1,233	732	2,766
Additions to property, plant and equipment	(44,358)	(40,004)	(40,344)
Net cash used by investing activities	(43,125)	(39,272)	(37,578)
<b>Cash flows from financing activities:</b>			
Payments for debt issuance costs	(1,684)	(3,342)	(4,467)
Additions to long-term debt	218,000	220,000	380,000
Payments of long-term debt	(295,800)	(124,800)	(530,279)
Proceeds from the sale of common stock	—	—	81,292
Proceeds from the issuance of common stock	3,192	10,734	9,290
Payment for the repurchase and retirement of common stock	—	(168,056)	—
Purchase of treasury stock	(10,943)	—	—
Payments for the repurchase of common stock warrants	—	(5,187)	(19,961)
Payments for common stock offering expenses of selling shareholders	—	(879)	(764)
Net cash used by financing activities	(87,235)	(71,530)	(84,889)
Net increase (decrease) in cash and cash equivalents	946	(7,091)	(7,047)
Cash and cash equivalents at beginning of period	12,274	19,365	26,412
Cash and cash equivalents at end of period	\$ 13,220	\$ 12,274	\$ 19,365
<b>Supplemental Disclosure:</b>			
Cash payments for income taxes, net	\$ 49,889	\$ 40,639	\$ 33,126
Cash payments for interest	\$ 42,974	\$ 40,707	\$ 37,960

See accompanying notes to consolidated financial statements.

**CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY**

<i>(Dollars in thousands)</i>	<i>Common Stock</i>	<i>Paid-In Capital</i>	<i>Retained Earnings</i>	<i>Treasury Stock</i>	<i>Total</i>
Balance December 31, 1995	\$ 50,120	\$ 218,156	\$ 32,880	\$ —	\$301,156
Net earnings			46,805		46,805
Common stock activity:					
Sale of common stock— 10,000,000 shares	10,000	71,292			81,292
Stock option grants and exercises (Note 6)	85	2,309			2,394
Warrant exercises – 1,227,052 shares	1,227	7,522			8,749
Warrant purchases – 3,578,399 shares		(19,961)			(19,961)
Common stock offering expenses of selling shareholders		(764)			(764)
Foreign currency translations			(14)		(14)
Balance December 31, 1996	61,432	278,554	79,671	—	419,657
Net earnings			67,053		67,053
Common stock activity:					
Repurchase of common stock— 10,842,299 shares	(10,842)	(157,214)			(168,056)
Stock option exercises (Note 6)	174	1,302			1,476
Warrant exercises – 1,298,498 shares	1,298	7,960			9,258
Warrant purchases – 650,071 shares		(5,187)			(5,187)
Retirement of common stock— 58,824 shares	(59)	59			—
Common stock offering expenses of selling shareholders		(879)			(879)
Balance December 31, 1997	52,003	124,595	146,724	—	323,322
Net earnings			97,938		97,938
Common stock activity:					
Stock option exercises (Note 6)	274	2,918			3,192
Purchase of treasury stock— 525,000 shares			(10,943)		(10,943)
Balance December 31, 1998	\$ 52,277	\$ 127,513	\$244,662	\$ (10,943)	\$413,509

See accompanying notes to consolidated financial statements.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands except per share data)

### NOTE 1 | THE COMPANY

Furniture Brands International, Inc. (referred to herein as the "Company") is the largest home furniture manufacturer in the United States. During the year ended December 31, 1998, the Company had three primary operating subsidiaries: Broyhill Furniture Industries, Inc.; Lane Furniture Industries, Inc.; and Thomasville Furniture Industries, Inc.

Substantially all of the Company's sales are made to unaffiliated furniture retailers. The Company has a diversified customer base with no one customer accounting for 10% or more of consolidated net sales and no particular concentration of credit risk in one economic section. Foreign operations and net sales are not material.

### NOTE 2 | SIGNIFICANT ACCOUNTING POLICIES

The significant accounting policies of the Company are set forth below.

#### *Use of Estimates*

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reported period. Actual results could differ from those estimates.

#### *Principles of Consolidation*

The consolidated financial statements include the accounts of the Company and all of its subsidiaries. All material intercompany transactions are eliminated in consolidation. The Company's fiscal year ends on December 31. The operating companies included in the consolidated financial statements report their results of operations as of the Saturday closest to December 31. Accordingly, the results of operations will periodically include a 53-week fiscal year. Fiscal years 1998, 1997 and 1996 were 52-week, 53-week and 52-week years, respectively.

#### *Cash and Cash Equivalents*

The Company considers all short-term investments with an original maturity of three months or less to be cash equivalents. Short-term investments are recorded at amortized cost, which approximates market.

#### *Inventories*

Inventories are stated at the lower of cost (first-in, first-out) or market.

#### *Property, Plant and Equipment*

Property, plant and equipment are recorded at cost when acquired. Depreciation is calculated using both accelerated and straight-line methods based on the estimated useful lives of the respective assets, which generally range from 3 to 45 years for buildings and improvements and from 3 to 12 years for machinery and equipment.

#### *Intangible Assets*

The excess of cost over net assets acquired in connection with the acquisition of Thomasville totaled \$93,110. This intangible asset is being amortized on a straight-line basis over a 40-year period.

The Company emerged from Chapter 11 reorganization effective with the beginning of business on August 3, 1992. In accordance with generally accepted accounting principles, the

Company was required to adopt "fresh-start" reporting which included adjusting all assets and liabilities to their fair values as of the effective date. The ongoing impact of the adoption of fresh-start reporting is reflected in the financial statements for all years presented.

As a result of adopting fresh-start reporting, the Company recorded reorganization value in excess of amounts allocable to identifiable assets of approximately \$146,000. This intangible asset is being amortized on a straight-line basis over a 20-year period.

Also in connection with the adoption of fresh-start reporting, the Company recorded approximately \$156,800 in fair value of trademarks and trade names based upon an independent appraisal. Such trademarks and trade names are being amortized on a straight-line basis over a 40-year period.

Long-lived assets are reviewed for impairment whenever events or changes in business circumstances indicate the carrying value of the assets may not be recoverable. Impairment losses are recognized if expected future cash flows of the related assets are less than their carrying values.

#### *Fair Value of Financial Instruments*

The Company considers the carrying amounts of cash and cash equivalents, receivables and accounts payable to approximate fair value because of the short maturity of these financial instruments.

Amounts outstanding under long-term debt agreements are considered to be carried on the financial statements at their estimated fair values because they were entered into recently and/or accrue interest at rates which generally fluctuate with interest rate trends.

Interest rate swap agreements used by the Company to fix the interest rate on a portion of its floating rate long-term debt are accounted for on the accrual basis. Amounts to be paid or received under the interest rate swap agreements are recognized in income as adjustments to interest expense. The book value of the interest rate swap agreements at December 31, 1998 exceeded the fair value by approximately \$5.5 million. The fair value of the interest rate swap agreements is based upon market quotes from the counterparties.

#### *Revenue Recognition*

The Company recognizes revenue when finished goods are shipped with appropriate provisions for returns and uncollectible accounts.

#### *Income Taxes*

Deferred tax assets and liabilities are recognized for the estimated future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates in effect for the year in which those temporary differences are expected to be recovered or settled. The effect of a change in tax rates on deferred tax assets and liabilities is recognized in income in the period that includes the enactment date.

#### *Stock-Based Compensation*

The Company accounts for stock-based compensation using the intrinsic value method prescribed in Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees."

#### *Reclassification*

Certain 1997 and 1996 amounts have been reclassified to conform to the 1998 presentation.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

### NOTE 3 | INVENTORIES

Inventories are summarized as follows:

	December 31, 1998	December 31, 1997
Finished products	\$122,993	\$118,385
Work-in-process	57,915	53,536
Raw materials	126,474	115,125
	<b>\$307,382</b>	<b>\$287,046</b>

### NOTE 4 | INTANGIBLE ASSETS

Intangible assets include the following:

	December 31, 1998	December 31, 1997
<b>Intangible assets, at cost:</b>		
Reorganization value in excess of amounts allocable to identifiable assets	\$146,063	\$146,063
Trademarks and trade names	156,828	156,828
Excess of cost over net assets acquired	93,110	93,110
	<b>396,001</b>	<b>396,001</b>
Less accumulated amortization	79,003	65,452
	<b>\$316,998</b>	<b>\$330,549</b>

### NOTE 5 | LONG-TERM DEBT

Long-term debt consists of the following:

	December 31, 1998	December 31, 1997
<b>Secured credit agreement:</b>		
Revolving credit facility	\$370,000	\$235,000
Term loan facility	200,000	200,000
Receivables securitization facility	—	220,000
Other	19,200	12,800
	<b>\$589,200</b>	<b>\$667,800</b>

The following discussion summarizes certain provisions of the long-term debt.

#### *Secured Credit Agreement*

The Secured Credit Agreement consists of a revolving credit facility and a term loan facility. The revolving credit facility is a five-year facility with an initial commitment of \$475,000. On July 14, 1998, the Company terminated its Receivable Securitization Facility. On this date the Company also amended its Secured Credit Agreement to increase the revolving credit facility commitment to \$600,000 from \$475,000 and to eliminate the interim commitment reduction dates. The revolving credit facility allows for issuance of letters of credit and cash borrowings. Letter of credit outstandings are limited to no more than \$60,000, with cash borrowings limited only by the facility's maximum availability less letters of credit outstanding.

Under the letter of credit facility, a fee of 0.875% per annum (subject to reduction based upon the Company achieving certain leverage ratios) is assessed for the account of the lenders ratably. A further fee of 0.125% is assessed on standby letters of credit representing a facing

fee. A customary administrative charge for processing letters of credit is also payable to the relevant issuing bank. Letter of credit fees are payable quarterly in arrears.

Cash borrowings under the revolving credit facility bear interest at a base rate or at London Interbank Offered Rate (LIBOR) plus an applicable margin which varies, depending upon the type of loan the Company executes. The applicable margin over the base rate and LIBOR is subject to adjustment based upon achieving certain leverage ratios. At December 31, 1998, all loans outstanding under the revolving credit facility were based on the LIBOR rate, for a weighted average interest rate of 5.85%.

At December 31, 1998, there were \$370,000 of cash borrowings and \$40,970 in letters of credit outstanding under the revolving credit facility, leaving an excess of \$189,030 available under the facility.

The revolving credit facility has no mandatory principal payments; however, the commitment matures on September 15, 2001. In addition, the facility requires principal payments from a portion of the net proceeds realized from (i) the sale, conveyance or other disposition of collateral securing the debt, or (ii) the sale by the Company for its own account of additional subordinated debt and/or shares of its preferred and/or common stock.

On June 27, 1997, the Company amended the Secured Credit Agreement to include a new term loan facility of \$200,000. The term loan facility is a non-amortizing ten-year facility, bearing interest at a base rate plus 0.75% or at LIBOR rate plus 1.75%, depending upon the type of loan the Company executes. At December 31, 1998, all loans outstanding under the term loan facility were based on the LIBOR rate for an interest rate of 6.75%.

The common stock of the Company's principal subsidiaries and substantially all of the Company's assets have been pledged or mortgaged as security for the Secured Credit Agreement. (Due to achieving certain leverage ratio requirements as of December 31, 1998, the mortgages on the Company's property, plant and equipment have been released.) The Secured Credit Agreement defines events of default and contains a number of restrictive covenants, including covenants limiting capital expenditures and incurrence of debt, and requires the Company to achieve certain financial ratios, some of which become more restrictive over time.

#### *Other*

Other long-term debt consists of various industrial revenue bonds with interest rates ranging from approximately 4.0% to 9.0%. Mandatory principal payments are required through 2004.

#### *Interest Rate Swap Agreements*

The Company has entered into various interest rate swap agreements to reduce the impact of changes in interest rates on its floating rate long-term debt. The following table summarizes the terms of the interest rate swap agreements in effect during 1998.

<i>Notional Amount</i>	<i>Maturity Date</i>	<i>Fixed Rate</i>	<i>Floating Rate</i>
\$100,000	February 1999	5.14%	3-month LIBOR
\$200,000	February 1999	5.14%	3-month LIBOR
\$300,000	January 2002	5.50%	3-month LIBOR

The swap agreements effectively convert the Company's floating rate long-term debt to a fixed rate. The Company pays the counterparties the fixed rate and receives payments based upon the floating rate. The Company is exposed to credit loss in the event of nonperformance by the counterparties; however, nonperformance is not anticipated.

*Other Information*

Maturities of long-term debt are \$0, \$0, \$370,000, \$0 and \$0 for years 1999 through 2003, respectively.

**NOTE 6 | COMMON STOCK**

The Company's restated certificate of incorporation includes authorization to issue up to 100.0 million shares of common stock with a \$1.00 per share stated value. As of December 31, 1998, 52,277,066 shares of common stock were issued and outstanding. It is not presently anticipated that dividends will be paid on common stock in the foreseeable future and certain of the debt instruments to which the Company is a party restrict the payment of dividends.

In October 1998, the Board of Directors authorized the repurchase of up to \$30,000 of the Company's common stock over the next twelve months. As of December 31, 1998, the Company has repurchased 525,000 shares for \$10,943.

Shares of common stock were reserved for the following purposes at December 31, 1998:

	Number of Shares
Common stock options:	
Granted	4,018,581
Available for grant	830,609
	<b>4,849,190</b>

Under the Company's 1992 Stock Option Plan, certain key employees may be granted nonqualified options, incentive options or combinations thereof. Nonqualified and incentive options may be granted to expire up to ten years after the date of grant. Options granted become exercisable at varying dates depending upon the passage of certain time periods.

The 1992 Stock Option Plan authorizes grants of options to purchase common shares at less than fair market value on the date of grant. During 1996, option grants totaling 217,978 common shares were made by the Company at less than market value. These options were issued to Thomasville employees as compensation for forfeited deferred compensation plans due to the acquisition; therefore, the cost of issuing the options at less than market value was included in determining the excess of cost over net assets acquired.

Changes in options granted and outstanding are summarized as follows:

	Year Ended December 31,					
	1998		1997		1996	
	Shares	Average Price	Shares	Average Price	Shares	Average Price
Beginning of period	3,897,930	\$ 7.48	3,859,476	\$ 6.63	2,498,000	\$4.75
Granted	436,500	23.02	292,500	16.36	1,620,926	9.14
Exercised	(273,546)	4.81	(173,964)	3.93	(85,050)	3.99
Cancelled	(42,303)	5.56	(80,082)	6.62	(174,400)	4.29
End of period	4,018,581	\$ 9.37	3,897,930	\$ 7.48	3,859,476	\$6.63
Exercisable at end of period	2,261,639		1,979,287		1,473,600	
Weighted average fair value of options granted		\$11.04		\$ 7.54		\$4.79

Had compensation cost for the Company's stock-based compensation plan been determined consistent with SFAS No. 123, the Company's net earnings and net earnings per share would have been as follows:

	Year Ended December 31,		
	1998	1997	1996
Net earnings			
As reported	\$97,938	\$67,053	\$46,805
Pro forma	96,180	65,907	46,112
Net earnings per share - basic			
As reported	\$ 1.88	\$ 1.19	\$ 0.79
Pro forma	1.85	1.17	0.78
Net earnings per share - diluted			
As reported	\$ 1.82	\$ 1.15	\$ 0.76
Pro forma	1.80	1.13	0.75

The weighted average fair value of options granted is estimated as of the date of grant using the Black-Scholes option pricing model with the following weighted average assumptions: risk free interest rate of 5.50%, 6.00% and 6.00% in 1998, 1997 and 1996, respectively; expected dividend yield of 0% for all years; expected life of 7 years for all years and expected volatility of 35%, 30% and 31% for 1998, 1997 and 1996 respectively.

Summarized information regarding stock options outstanding and exercisable at December 31, 1998 follows:

Range of Exercise Prices	Outstanding			Exercisable	
	Shares	Average Contractual Life	Average Price	Shares	Average Price
Up to \$10	2,584,581	4.4	\$ 5.63	1,921,139	\$ 5.10
\$10 - \$20	1,042,500	6.9	12.72	329,500	12.26
Over \$20	391,500	8.1	25.17	11,000	21.00
	4,018,581	5.4	\$ 9.37	2,261,639	\$ 6.22

Effective December 31, 1997, the Company adopted SFAS No. 128, "Earnings per Share." SFAS No. 128 requires a reconciliation of the numerator and denominator of the net earnings per common share calculations for all periods presented. The numerator for basic and diluted net earnings per common share is net earnings for all periods presented. The denominator for basic and diluted net earnings per common share for 1998, 1997 and 1996 follows:

	Year Ended December 31,		
	1998	1997	1996
Weighted average shares used for basic net earnings per common share	52,095,451	56,438,465	59,172,153
Effect of dilutive securities:			
Stock options	1,713,515	1,447,624	1,052,852
Warrants	—	587,105	1,721,448
Weighted average shares used for diluted net earnings per common share	53,808,966	58,473,194	61,946,453

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

At December 31, 1996, the Company had outstanding approximately 2.0 million warrants to purchase common stock at \$7.13 per share. The warrants, which included a five-year call protection which expired on August 3, 1997, were redeemed on August 15, 1997.

NOTE 7 | INCOME TAXES

Income tax expense was comprised of the following:

	Year Ended December 31,		
	1998	1997	1996
Current:			
Federal	\$46,257	\$43,680	\$ 40,870
State and local	5,324	4,577	4,014
	51,581	48,257	44,884
Deferred	2,624	(8,056)	(10,814)
	\$54,205	\$40,201	\$ 34,070

The following table reconciles the differences between the federal corporate statutory rate and the Company's effective income tax rate:

	Year Ended December 31,		
	1998	1997	1996
Federal corporate statutory rate	35.0%	35.0%	35.0%
State and local income taxes, net of federal tax benefit	1.8	2.3	2.3
Amortization of excess reorganization value	1.7	2.4	2.9
Other	(2.9)	(2.2)	(1.6)
<b>Effective income tax rate</b>	<b>35.6%</b>	<b>37.5%</b>	<b>38.6%</b>

The sources of the tax effects for temporary differences that give rise to the deferred tax assets and liabilities were as follows:

	December 31, 1998	December 31, 1997
Deferred tax assets:		
Expense accruals	\$ 20,296	\$ 18,855
Valuation reserves	6,737	8,190
Employee postretirement benefits other than pensions	3,134	3,648
Inventory costs capitalized	3,429	3,367
Employee pension plans	2,139	1,109
Other	1,648	2,208
<b>Total gross deferred tax assets</b>	<b>37,383</b>	<b>37,377</b>
Valuation allowance	—	—
<b>Total net deferred tax assets</b>	<b>37,383</b>	<b>37,377</b>
Deferred tax liabilities:		
Fair value adjustments	(73,867)	(76,558)
Depreciation	(7,924)	(5,535)
Fair market value adjustments	(7,421)	(4,631)
Other	(10,327)	(10,185)
<b>Total deferred tax liabilities</b>	<b>(99,539)</b>	<b>(96,909)</b>
Net deferred tax liabilities	\$(62,156)	\$(59,532)

The net deferred tax liabilities are included in the consolidated balance sheet as follows:

	<i>December 31, 1998</i>	<i>December 31, 1997</i>
Prepaid expenses and other current assets	\$ 24,914	\$ 19,214
Other long-term liabilities	(87,070)	(78,746)
	<b><u>\$(62,156)</u></b>	<b><u>\$(59,532)</u></b>

**NOTE 8 | EMPLOYEE BENEFITS**

The Company sponsors or contributes to retirement plans covering substantially all employees. The total cost of all plans for 1998, 1997 and 1996 was \$7,773, \$8,412 and \$9,450, respectively.

*Company-Sponsored Defined Benefit Plans*

Annual cost for defined benefit plans is determined using the projected unit credit actuarial method. Prior service cost is amortized on a straight-line basis over the average remaining service period of employees expected to receive benefits.

It is the Company's practice to fund pension costs to the extent that such costs are tax deductible and in accordance with ERISA. The assets of the various plans include corporate equities, government securities, corporate debt securities and insurance contracts. The table below summarizes the funded status of the Company-sponsored defined benefit plans.

	<i>December 31, 1998</i>	<i>December 31, 1997</i>
<b>Change in projected benefit obligation:</b>		
Projected benefit obligation – beginning of year	\$273,487	\$262,667
Service cost	7,419	7,120
Interest cost	19,856	19,026
Actuarial gain	168	57
Benefits paid	(16,432)	(15,383)
Projected benefit obligation – end of year	\$284,498	\$273,487
<b>Change in plan assets:</b>		
Fair value of plan assets – beginning of year	\$306,797	\$279,054
Actual return on plan assets	41,591	42,531
Employer contributions	585	595
Benefits paid	(16,432)	(15,383)
Fair value of plan assets – end of year	\$332,541	\$306,797
Funded status	\$ 48,043	\$ 33,310
Unrecognized net gain	(49,236)	(33,558)
Unrecognized prior service cost	975	978
Prepaid (accrued) pension cost	\$ (218)	\$ 730

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Net periodic pension cost for 1998, 1997 and 1996 included the following components:

	Year Ended December 31,		
	1998	1997	1996
Service cost-benefits earned during the period	\$ 7,419	\$ 7,120	\$ 6,792
Interest cost on the projected benefit obligation	19,856	19,026	18,102
Expected return on plan assets	(25,464)	(23,115)	(20,886)
Net amortization and deferral	(224)	212	246
<b>Net periodic pension cost</b>	<b>\$ 1,587</b>	<b>\$ 3,243</b>	<b>\$ 4,254</b>

Employees are covered primarily by noncontributory plans, funded by Company contributions to trust funds, which are held for the sole benefit of employees. Monthly retirement benefits are based upon service and pay with employees becoming vested upon completion of five years of service.

The expected long-term rate of return on plan assets was 8.5% in 1998, 1997 and 1996. Measurement of the projected benefit obligation was based upon a weighted average discount rate of 7.25% and a long-term rate of compensation increase of 4.5% for all years presented.

*Other Retirement Plans and Benefits*

In addition to defined benefit plans, the Company makes contributions to defined contribution plans and sponsors employee savings plans. The cost of these plans is included in the total cost for all plans reflected above.

**NOTE 9 | EXTRAORDINARY ITEM – EARLY EXTINGUISHMENT OF DEBT**

In conjunction with the September 6, 1996 refinancing of the Secured Credit Agreement, the Company charged to results of operations \$7,417, net of tax benefit of \$4,469, representing the deferred financing fees and expenses pertaining to the refinanced facility. The charge was recorded as an extraordinary item.

**NOTE 10 | COMMITMENTS AND CONTINGENT LIABILITIES**

Certain of the Company's real properties and equipment are operated under lease agreements. Rental expense under operating leases totaled \$16,537, \$15,699 and \$14,758 for 1998, 1997 and 1996, respectively. Annual minimum payments under operating leases are \$12,980, \$9,600, \$6,577, \$5,352 and \$4,111 for 1999 through 2003, respectively.

The Company is or may become a defendant in a number of pending or threatened legal proceedings in the ordinary course of business. In the opinion of management, the ultimate liability, if any, of the Company from all such proceedings will not have a material adverse effect upon the consolidated financial position or results of operations of the Company and its subsidiaries.

**NOTE 11 | QUARTERLY FINANCIAL INFORMATION (UNAUDITED)**

Following is a summary of unaudited quarterly information:

	<i>Fourth Quarter</i>	<i>Third Quarter</i>	<i>Second Quarter</i>	<i>First Quarter</i>
<b>Year ended December 31, 1998:</b>				
Net sales	\$497,628	\$487,178	\$470,146	\$505,298
Gross profit	130,996	128,258	125,435	130,823
Net earnings	\$ 24,669	\$ 30,548	\$ 21,107	\$ 21,614
Net earnings per common share:				
Basic	\$ 0.48	\$ 0.58	\$ 0.40	\$ 0.41
Diluted	\$ 0.46	\$ 0.57	\$ 0.39	\$ 0.40
Common stock price range:				
High	\$ 27 $\frac{1}{4}$	\$ 30 $\frac{1}{16}$	\$ 33 $\frac{1}{16}$	\$ 32 $\frac{1}{16}$
Low	\$ 13 $\frac{1}{2}$	\$ 19 $\frac{1}{2}$	\$ 23 $\frac{1}{16}$	\$ 19 $\frac{1}{16}$
<b>Year ended December 31, 1997:</b>				
Net sales	\$473,597	\$440,666	\$444,152	\$449,861
Gross profit	116,738	107,803	112,724	113,425
Net earnings	\$ 18,865	\$ 14,614	\$ 16,515	\$ 17,059
Net earnings per common share:				
Basic	\$ 0.36	\$ 0.28	\$ 0.27	\$ 0.28
Diluted	\$ 0.35	\$ 0.27	\$ 0.26	\$ 0.27
Common stock price range:				
High	\$ 21 $\frac{1}{8}$	\$ 21	\$ 19 $\frac{1}{8}$	\$ 15 $\frac{1}{8}$
Low	\$ 15 $\frac{1}{8}$	\$ 17 $\frac{1}{2}$	\$ 14 $\frac{1}{8}$	\$ 13 $\frac{1}{8}$

The Company has not paid cash dividends on its common stock during the three years ended December 31, 1998. The closing market price of the Company's common stock on December 31, 1998 was \$27.25 per share.

INDEPENDENT AUDITORS' REPORT

The Board of Directors and Shareholders  
Furniture Brands International, Inc.:

We have audited the accompanying consolidated balance sheets of Furniture Brands International, Inc. and subsidiaries as of December 31, 1998 and 1997, and the related consolidated statements of operations, shareholders' equity, and cash flows for each of the years in the three-year period ended December 31, 1998. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Furniture Brands International, Inc. and subsidiaries as of December 31, 1998 and 1997, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 1998, in conformity with generally accepted accounting principles.

**KPMG LLP**

St. Louis, Missouri

January 29, 1999

FIVE-YEAR CONSOLIDATED FINANCIAL REVIEW

(Dollars in thousands except per share data)	Year Ended December 31,				
	1998	1997	1996	1995 <sup>1</sup>	1994
<b>Summary of operations:</b>					
Net sales	\$1,960,250	\$1,808,276	\$1,696,795	\$1,073,889	\$1,072,696
Gross profit	515,512	450,690	431,473	291,237	298,712
Interest expense	43,455	42,747	45,217	33,845	37,886
Earnings before income tax expense, discontinued operations and extraordinary item	152,143	107,254	88,292	57,038	48,841
Income tax expense	54,205	40,201	34,070	22,815	20,908
Earnings from continuing operations	97,938 <sup>3</sup>	67,053	54,222	34,223 <sup>2</sup>	27,933
Discontinued operations	—	—	—	—	10,339
Extraordinary item	—	—	(7,417)	(5,815)	—
Net earnings	\$ 97,938	\$ 67,053	\$ 46,805	\$ 28,408	\$ 38,272
<b>Per share of common stock — diluted:</b>					
Earnings from continuing operations	\$ 1.82 <sup>3</sup>	\$ 1.15	\$ 0.88	\$ 0.67 <sup>2</sup>	0.54
Discontinued operations	—	—	—	—	0.20
Extraordinary item	—	—	(0.12)	(0.11)	—
Net earnings	\$ 1.82	\$ 1.15	\$ 0.76	\$ 0.56	\$ 0.74
<b>Weighted average common shares — diluted (in thousands)</b>					
	53,809	58,473	61,946	50,639	51,495
<b>Other information (continuing operations):</b>					
Working capital	\$ 509,148	\$ 482,288	\$ 462,661	\$ 455,036	\$ 308,323
Property, plant and equipment, net	293,777	294,061	301,962	306,406	181,393
Capital expenditures	44,358	40,004	40,344	35,616	21,108
Total assets	1,303,204	1,257,236	1,269,204	1,291,739	881,735
Long-term debt	589,200	667,800	572,600	705,040	409,679
Shareholders' equity	\$ 413,509	\$ 323,322	\$ 419,657	\$ 301,156	\$ 275,394

<sup>1</sup>On December 31, 1995 the Company purchased Thomasville. The Company's results of operations for 1995 do not include any of the operations of Thomasville, since the acquisition occurred as of the last business day of the year.

<sup>2</sup>Earnings from continuing operations before gain on insurance settlement, net of income tax expense, and earnings per common share from continuing operations before gain on insurance settlement, net of income tax expense, were \$29,463 and \$0.58, respectively.

<sup>3</sup>Earnings from continuing operations before nonrecurring gain, net of income tax expense, and earnings per common share from continuing operations before nonrecurring gain, net of income tax expense, were \$90,077 and \$1.67, respectively.

## BOARD OF DIRECTORS

**Katherine Button Bell** <sup>2</sup>  
*President of Button Brand  
Development, Inc.*

**Wilbert G. Holliman** <sup>1</sup>  
*Chairman of the Board, President and  
Chief Executive Officer of the Company*

**Bruce A. Karsh** <sup>2, 3</sup>  
*President of Oaktree Capital  
Management, LLC*

**Brent B. Kincaid**  
*Retired President and Chief Executive  
Officer of Broyhill Furniture  
Industries, Inc.*

**Donald E. Lasater** <sup>1, 3</sup>  
*Retired Chairman of the Board and  
Chief Executive Officer of  
Mercantile Bancorporation Inc.*

**Lee M. Liberman** <sup>2\*, 3</sup>  
*Retired Chairman of the Board and  
Chief Executive Officer of  
Laclede Gas Company*

**Richard B. Loynd** <sup>1\*</sup>  
*Retired Chairman of the Board  
of the Company*

**Malcolm Portera** <sup>2</sup>  
*President of Mississippi State University*

**Albert E. Suter** <sup>1, 3\*</sup>  
*Senior Vice Chairman of  
Emerson Electric Co.*

### Committees of the Board

<sup>1</sup>*Executive Committee*

<sup>2</sup>*Audit Committee*

<sup>3</sup>*Executive Compensation and Stock  
Option Committee  
(\*indicates Committee Chairman)*

## PRINCIPAL CORPORATE OFFICERS

**Wilbert G. Holliman**  
*Chairman of the Board, President and  
Chief Executive Officer*

**David P. Howard**  
*Vice-President, Treasurer and  
Chief Financial Officer*

**Lynn Chipperfield**  
*Vice-President, General Counsel  
and Secretary*

**Steven W. Alstadt**  
*Controller and Chief Accounting Officer*

## PRESIDENTS OF OPERATING COMPANIES

**Dennis R. Burgette**  
*Broyhill Furniture Industries, Inc.*

**John T. Foy**  
*Action Industries, Inc.\**

**Christian J. Pfaff**  
*Thomasville Furniture Industries, Inc.*

*\*Subsidiary of Lane Furniture  
Industries, Inc.*

## INVESTOR INFORMATION

**Transfer Agent and Registrar for  
Common Stock**  
*The Bank of New York  
Church Street Station  
New York, New York 10286  
(800) 524-4458*

**Exchange Listing**  
*Common shares are listed on the  
New York Stock Exchange  
(trading symbol: FBN)*

**Corporate Offices**  
*101 South Hanley Road  
St. Louis, Missouri 63105-3493  
(314) 863-1100*

**Annual Meeting**  
*The Annual Meeting of Shareholders will  
be at 9:00 a.m. on Thursday, April 29,  
1999, at the Ritz-Carlton Hotel, 100  
Carondelet Plaza, St. Louis, Missouri.*

**Form 10-K Annual Report**  
*Shareholders may obtain a copy of  
the current Form 10-K filed with the  
Securities and Exchange Commission  
by writing to the Treasurer of  
Furniture Brands International  
at the Corporate Offices.*

**Independent Auditors**  
*KPMG LLP  
10 S. Broadway, Suite 900  
St. Louis, Missouri 63102-1761  
(314) 444-1400*

**Internet Access**  
*Corporate news releases, Form 10-K  
and Form 10-Q, the annual report and  
other information about the Company  
and its subsidiaries are available through  
the Company's Internet Web site at:  
<http://www.furniturebrands.com>.*

*Furniture Brands International completes the breadth of its product offerings with full-line collections and selected niche products from the following divisions. These product offerings include premium upholstery collections, promotional and ready-to-assemble (RTA) products, and high-end office furniture.*



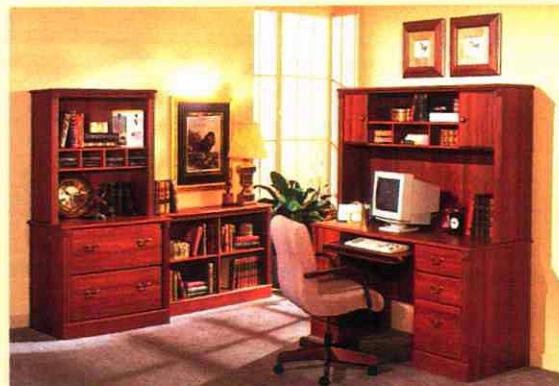
The Pearson Company



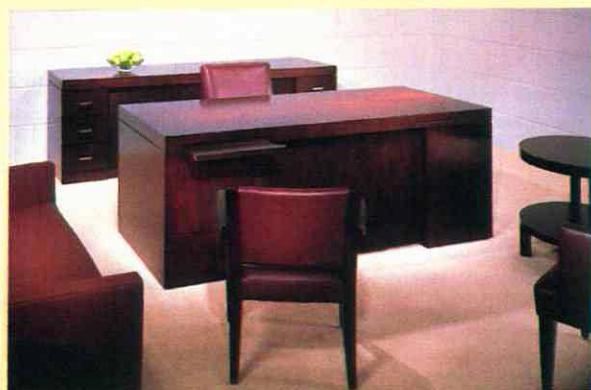
Highland House



Founders Furniture



Creative Interiors



HBF



*America's largest home furniture manufacturer*  
St. Louis, Missouri